

CIA/OCI/MEMO

Approved For Release 2000/09/14 : CIA-RDP86T00608R000300070049-0

~~CONFIDENTIAL~~ CONFIDENTIAL/NFD--PROSPECTS FOR THE LATIN
AMERICAN ECONOMIC SYSTEM

CIA 15APR75

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0544/75

No. 0544/75
April 15, 1975

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MEMORANDUM

SUBJECT: Prospects for the Latin American Economic System

Summary

The proposal for an exclusively Latin American economic system (SELA) has been greeted so far with considerable skepticism. Apart from its co-sponsors, Mexico and Venezuela, only a few governments seem eager to commit themselves. Even if it does not attract new adherents, however, some sort of regional cooperative is almost certain to be created before the year is out. A number of governments probably will join, perhaps for no better reason than to show support for Latin American solidarity.

To become more than just another in the long list of impotent regional organizations, SELA will have to overcome formidable hurdles. Old and new rivalries, competing national interests, and a concern that the organization could cause trouble with the US will temper commitment.

SELA's ambitious goals and planned staffing will require considerable financing. All members presumably will be required to pay dues. Although Venezuela and Mexico seem the most eager and therefore will probably be the principal underwriters, they are unlikely to provide more than a few million dollars. Even then, they will contribute only if they also have the key roles in determining what projects are to be undertaken and are assured of receiving a good return for their money. A number of governments, especially those in South America, already are suspicious of Venezuelan and Mexican pretensions to regional leadership. Some are wary of Cuba's participation.

The underlying purpose of the new organization is to develop the economies of Latin America and the Caribbean

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15 (1), (2) or (3) of the schedule	
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and to promote their unification. Though the mechanics have not been determined, the stated goals are to channel capital into economic development projects, encourage Latin American-controlled multinational enterprises, defend prices and ensure markets for raw materials and manufactured goods, increase the supply of food, exchange technology, and promote arrangements with other regional organizations. A more general objective will be to provide an informal vehicle for governments to pool and coordinate research and knowledge on economic issues affecting common Latin interests.

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Whatever form it takes, SELA will press for better economic treatment from the industrialized countries, principally the US. Discontent with US policies toward Latin America and the less developed world is broad, and many governments might be attracted to participate if they see a means of lobbying successfully for trade and other concessions from the US. But economic and political realities in the hemisphere will make it difficult for the potential members to agree on how to solve their individual problems in a coordinated manner. Most governments agree that some method must be found to create a "new international economic order," but they will have to be assured that an organization of the type proposed can do it and do it in a way that is consistent with their national interests.

Reception

Apart from its two co-sponsors, the only enthusiasm has come from the Castro government, which views SELA as a mechanism for putting pressure on the US to make political and economic concessions to Cuba and the rest of Latin America. Castro has long believed that the only way to get concessions from the US is by confronting Washington with a united Latin America. The new organization will allow Cuba to identify with the hemisphere without abdicating what it has stood for during the last decade of political and economic isolation. Castro probably

also believes that SELA could complement his bilateral efforts to re-establish political relations with the Latin nations. Cuba has been advocating Latin-only forums for some time and seems to have played a key role in planting this latest idea. Even so, the Castro government does not want to assume a leading role, at least at the outset, for fear this would damage the organization's chances.

Peru and Panama are guardedly enthusiastic. The concept is in line with Peru's support for organizations that promote Latin American economic integration and the Velasco government would probably join for that reason alone. Wariness of Venezuelan and Mexican leadership aspirations, however, will temper Peru's enthusiasm and will prompt Lima to look closely at the actual benefits it could gain. Panama also would probably climb aboard if only to further the Third World-oriented image General Torrijos is portraying. The Panamanians will want, however, to be assured that they would not be harming their chances in the canal negotiations.

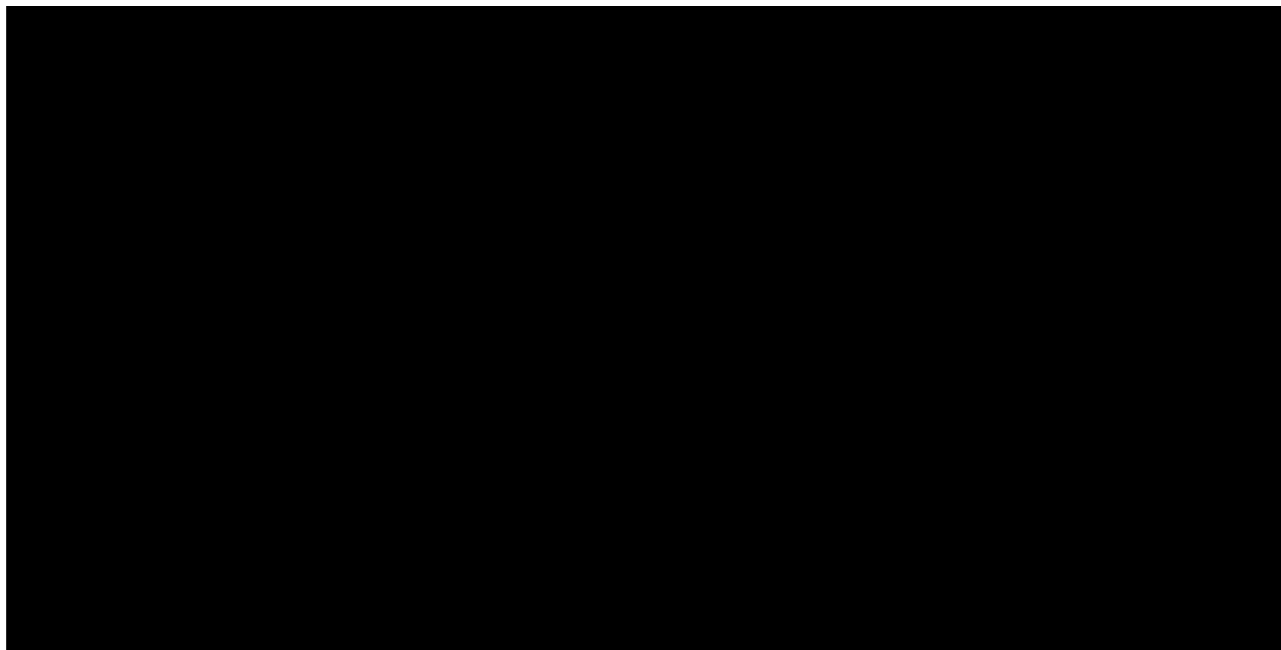
The remaining countries are less enthusiastic for a variety of reasons. Their reactions range from mild skepticism to outright rejection. All share the same reservations about the proposal: wariness of Mexican and Venezuelan intentions, doubts about its economic feasibility, concern that it could cause political and economic difficulties with the US, and concern that it would try to replace the OAS or other existing regional organizations. Mexico and Venezuela have been doing their utmost to convince Latin American and Caribbean governments that these concerns are groundless, but they have not had nor are they likely to have much success. All the governments have made politely favorable responses, but they simply are not likely to commit themselves until they determine exactly what tangible benefits they can gain, and ensure that they are furthering their national interests.

The larger countries are curious, but skepticism and uncertainties prevail. Brazil, for example, would not support SELA if it appeared to be a forum for confrontation with the US. Brazil prefers to work bilaterally with the US to preserve what it perceives as its preferred relationship, but it will not close the door if it concludes that SELA can benefit its economy. Argentina has serious doubts about the efficacy of the organization, and probably suspects Venezuelan and Mexican motives. Other South American nations, such as Chile, Colombia, Uruguay, Ecuador, and Bolivia, are also non-committal. They would probably join, following the initiative of others, but they are not likely to participate

actively without first being assured that the organization will benefit them and not create troubles with the US.

Central American and Caribbean countries are the most reluctant. They have close bilateral economic and political ties with the US and are concerned not to damage them. The governments in this area may also believe that their own regional organizations, such as the Central American and Caribbean common markets, might suffer from the presence of a group like SELA.

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Prospects

Most reports indicate that one of SELA's first attempts at actually doing something will be in the area of government-to-government joint ventures. It will apparently set up machinery for Latin American governments to undertake joint development projects. Some projects will apparently be undertaken with countries outside of Latin America.

Some 40 to 50 joint projects, mostly in mining, petroleum and industry, have been discussed. Cooperative ventures like these need money to succeed. Raising it would presumably be the responsibility of the governments directly involved, but some governments might be expected to take the lead in footing the bills.

Venezuela is the most likely source of funds, although only to a limited extent. Despite its often expressed desire to aid the development of other developing countries and to

support other nations' efforts to boost prices of their commodity exports, Caracas is offering only limited support. Most of its surplus funds are now placed abroad in short-term deposits at commercial interest rates. In a few years, this money will probably be needed to finance a growing trade deficit. Only some \$40 to \$80 million in short-term loans was offered to the Central American nations for a coffee stockpiling scheme. Partial financing for oil sales that can be converted into 25-year development loans was recently initiated by Caracas for the five Central American countries and Panama.

The Venezuelans will want a key role in determining what projects SELA undertakes. Their experiences with unlikely schemes devised in the Latin American Energy Organization will cause them to look closely at any proposals. Caracas will be reluctant to be the sole financial backer, especially if it finds that the organization does not produce the desired benefit for Venezuela.

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Other than Venezuela and Mexico, few if any governments are likely to be able or willing to provide significant funds. SELA might well become increasingly attractive to other governments, however, if real economic benefits from its projects become apparent to them. Details are a long way from being worked out, but its boosters say it will undertake projects that are realistic and profitable. Previous efforts at regional integration were too ambitious; this one, its proponents say, will bite off something it can chew.

Implications for the US

A major objective of SELA is to defend prices and ensure markets for exports. At least one prominent spokesman, Mexico's Minister of National Properties Francisco Alejo, has acknowledged that the organization will try to follow the example

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of OPEC in defending the prices of Latin American raw materials. Although he and SELA's other advocates deny that the intention is to bring the organization into conflict with the US, the idea of applying the OPEC model to commodities other than oil has wide appeal. Some producer arrangements have been formed -- such as the banana cartel promoted last year by the Central Americans, and other organizations of producers of coffee and sugar -- but they have not been successful in manipulating markets or prices.

Most of the nations in the hemisphere, moreover, prefer not to get involved in an organization that could lead them into new trouble with the US over economic and political issues. They doubtless consider Secretary Kissinger's Houston speech on March 1 a clear warning against forming organizations that restrict access or artificially raise prices of raw materials to levels that cause serious disruption of the world economy.

Also, most Latin nations believe that the right conditions for cartels do not exist in Latin America. Brazil, for one, believes that the OPEC example is difficult to copy; it prefers that raw materials suppliers deal with consumer countries on mutually beneficial arrangements. Confrontation tactics, Brazil believes, will have to give way to more rational approaches. Other governments, aware of the political hazards and uncertain of the economic feasibility of forming cartels, will probably be as wary as Brazil.

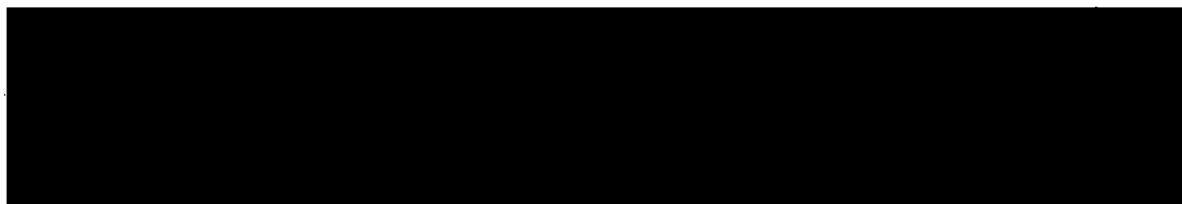
Even though the Latins are likely to balk at forming a group that might emulate OPEC tactics, they nevertheless will be attracted to the notion that, working together, they can extract economic concessions from the US. The success that the Third World has had in commanding the attention of developed nations has not gone unnoticed. They probably believe that through SELA they might be able to lobby for better prices for their raw materials and fewer restrictions in marketing them. They may also expect assistance on such issues as access to US technology and financial resources and to the capital of international lending institutions.

There is also a growing feeling, articulated most often by would-be Latin American leaders Echeverria and Perez, that unless some bold new pattern of unity and integration can be developed under the control of the dependent Latin nations, realistic options for economic development will remain painfully limited.

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Most Latin American nations probably agree with Echeverria, at least in theory. Latin America and the less developed world are dissatisfied with US policies toward them. They are seeking to mobilize themselves around a common cause against the developed states. Their desire to create a "new world economic order" that will unify them on key issues of underdevelopment is strong. In practice, however, the Latin American nations will want to know first what SELA can accomplish for them and what its approach will be before committing themselves to genuine participation. But even if SELA turns out to be more successful than now appears likely, there will be no rapid solutions to the continent's development problems.